

AMENDED IN ASSEMBLY MAY 4, 2010  
AMENDED IN ASSEMBLY FEBRUARY 22, 2010  
CALIFORNIA LEGISLATURE—2009–10 REGULAR SESSION

## ASSEMBLY BILL

**No. 1719**

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**Introduced by Assembly Member Harkey**  
**(~~Coauthor: Assembly Member Knight~~ Coauthors: Assembly**  
**Members Anderson, Knight, Miller, Nestande, and Villines)**

February 2, 2010

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An act to add and repeal Section 6377 of the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

### LEGISLATIVE COUNSEL'S DIGEST

AB 1719, as amended, Harkey. Sales and use taxes: exemption: business equipment.

The Sales and Use Tax Law imposes a tax on retailers measured by the gross receipts from the sale of tangible personal property sold at retail in this state, or on the storage, use, or other consumption in this state of tangible personal property purchased from a retailer for storage, use, or other consumption in this state. That law provides various exemptions from those taxes.

This bill would, *until January 1, 2017*, exempt from those taxes the sale of, and the storage, use, or other consumption in this state, of tangible personal property, as defined, purchased for use by a qualified person, as defined, primarily in any stage of manufacturing, processing, refining, fabricating, or recycling of property; in research and development; to maintain, repair, measure, or test specified property; and for use by a contractor purchasing that property as an agent or for

the contractor's own account and subsequent resale for use in a construction contract, as specified.

The Bradley-Burns Uniform Local Sales and Use Tax Law authorizes counties and cities to impose local sales and use taxes in conformity with the Sales and Use Tax Law, and the Transactions and Use Tax Law authorizes districts, as specified, to impose transactions and use taxes in conformity with the Sales and Use Tax Law. Exemptions from state sales and use taxes are incorporated in these laws.

This bill would specify that this exemption does not apply to local sales and use taxes, transactions and use taxes, and specified state taxes.

This bill would take effect immediately as a tax levy.

Vote: majority. Appropriation: no. Fiscal committee: yes.  
State-mandated local program: no.

*The people of the State of California do enact as follows:*

- 1     SECTION 1. Section 6377 is added to the Revenue and  
2     Taxation Code, to read:  
3     6377. (a) There are exempted from the taxes imposed by this  
4     part the gross receipts from the sale of, and the storage, use, or  
5     other consumption in this state of any of the following:  
6     (1) Tangible personal property purchased for use by a qualified  
7     person to be used primarily in any stage of the manufacturing,  
8     processing, refining, fabricating, or recycling of property,  
9     beginning at the point any raw materials are received by the  
10    qualified person and introduced into the process and ending at the  
11    point at which the manufacturing, processing, refining, fabricating,  
12    or recycling has altered property to its completed form, including  
13    packaging, if required.  
14    (2) Tangible personal property purchased for use by a qualified  
15    person to be used primarily in research and development.  
16    (3) Tangible personal property purchased for use by a qualified  
17    person to be used primarily to maintain, repair, measure, or test  
18    any property described in paragraph (1) or (2).  
19    (4) Tangible personal property purchased for use by a contractor  
20    purchasing that property either as an agent of a qualified person  
21    or for the contractor's own account and subsequent resale to a  
22    qualified person for use in the performance of a construction  
23    contract for the qualified person who will use the tangible personal  
24    property as an integral part of the manufacturing, processing,

1 refining, fabricating, or recycling process, or as a research or  
2 storage facility for use in connection with the manufacturing  
3 process.

4 This exemption shall not apply to any tangible personal property  
5 that is used primarily in administration, general management, or  
6 marketing.

7 (b) For purposes of this section:

8 (1) "Fabricating" means to make, build, create, produce, or  
9 assemble components or property to work in a new or different  
10 manner.

11 (2) "Manufacturing" means the activity of converting or  
12 conditioning property by changing the form, composition, quality,  
13 or character of the property for ultimate sale at retail or use in the  
14 manufacturing of a product to be ultimately sold at retail.  
15 Manufacturing includes any improvements to tangible personal  
16 property that result in a greater service life or greater functionality  
17 than that of the original property.

18 (3) "Primarily" means tangible personal property used 50 percent  
19 or more of the time in an activity described in subdivision (a).

20 (4) "Process" means the period beginning at the point at which  
21 any raw materials are received by the qualified taxpayer and  
22 introduced into the manufacturing, processing, refining, fabricating,  
23 or recycling activity of the qualified taxpayer and ending at the  
24 point at which the manufacturing, processing, refining, fabricating,  
25 or recycling activity of the qualified taxpayer has altered tangible  
26 personal property to its completed form, including packaging, if  
27 required. Raw materials shall be considered to have been  
28 introduced into the process when the raw materials are stored on  
29 the same premises where the qualified taxpayer's manufacturing,  
30 processing, refining, or recycling activity is conducted. Raw  
31 materials that are stored on premises other than where the qualified  
32 taxpayer's manufacturing, processing, refining, fabricating, or  
33 recycling activity is conducted, shall not be considered to have  
34 been introduced into the manufacturing, processing, refining,  
35 fabricating, or recycling process.

36 (5) "Processing" means the physical application of the materials  
37 and labor necessary to modify or change the characteristics of  
38 property.

39 (6) "Qualified person" means any person that is both of the  
40 following:

1 (A) A new trade or business. In determining whether a trade or  
2 business activity qualifies as a new trade or business, the following  
3 rules shall apply:

4 (i) In any case where a person purchases or otherwise acquires  
5 all or any portion of the assets of an existing trade or business  
6 (irrespective of the form of entity) that is doing business in this  
7 state (within the meaning of Section 23101), the trade or business  
8 thereafter conducted by that person (or any related person) shall  
9 not be treated as a new business if the aggregate fair market value  
10 of the acquired assets (including, real, personal, tangible, and  
11 intangible property) used by that person (or any related person) in  
12 the conduct of his or her trade or business—~~exceed~~ *exceeds* 20  
13 percent of the aggregate fair market value of the total assets of the  
14 trade or business being conducted by the person (or any related  
15 person). For purposes of this subparagraph only, the following  
16 rules shall apply:

17 (I) The determination of the relative fair market values of the  
18 acquired assets and the total assets shall be made as of the last day  
19 of the month following the quarterly period in which the person  
20 (or any related person) first uses any of the acquired trade or  
21 business assets in his or her business activity.

22 (II) Any acquired assets that constituted property described in  
23 Section 1221(a) of the Internal Revenue Code in the hands of the  
24 transferor shall not be treated as assets acquired from an existing  
25 trade or business, unless those assets also constitute property  
26 described in Section 1221(a) of the Internal Revenue Code in the  
27 hands of the acquiring person (or related person).

28 (ii) In any case where a person (or any related person) is engaged  
29 in one or more trade or business activities in this state, or has been  
30 engaged in one or more trade or business activities in this state  
31 within the preceding 36 months (“prior trade or business activity”),  
32 and thereafter commences an additional trade or business activity  
33 in this state, the additional trade or business activity shall only be  
34 treated as a new business if the additional trade or business activity  
35 is classified under a different division of the Standard Industrial  
36 Classification Manual published by the United States Office of  
37 Management and Budget, 1987 edition, than are any of the person’s  
38 (or any related person’s) current or prior trade or business activities  
39 in this state.

1 (iii) In any case where a person, including all related persons,  
2 is engaged in trade or business activities wholly outside of this  
3 state and that person first commences doing business in this state  
4 (within the meaning of Section 23101) after December 31, 1993  
5 (other than by purchase or other acquisition described in clause  
6 (i)), the trade or business activity shall be treated as a new business.

7 (iv) In any case where the legal form under which a trade or  
8 business activity is being conducted is changed, the change in form  
9 shall be disregarded and the determination of whether the trade or  
10 business activity is a new business shall be made by treating the  
11 person as having purchased or otherwise acquired all or any portion  
12 of the assets of an existing trade or business under the rules of  
13 clause (i).

14 (v) "Related person" means any person that is related to that  
15 person under either Section 267 or 318 of the Internal Revenue  
16 Code.

17 (vi) "Acquire" includes any gift, inheritance, transfer incident  
18 to divorce, or any other transfer, whether or not for consideration.

19 (B) Engaged in those lines of business described in Codes 2011  
20 to 3999, inclusive, of the Standard Industrial Classification Manual  
21 published by the United States Office of Management and Budget,  
22 1987 edition.

23 (7) Notwithstanding paragraph (6), "qualified person" shall not  
24 include any person who has conducted business activities in a new  
25 trade or business for three or more years.

26 (8) "Refining" means the process of converting a natural  
27 resource to an intermediate or finished product.

28 (9) "Research and development" means those activities that are  
29 described in Section 174 of the Internal Revenue Code or in any  
30 regulations thereunder.

31 (10) "Tangible personal property" does not include any of the  
32 following:

33 (A) Consumables with a normal useful life of less than one year,  
34 except as provided in subparagraph (E) of paragraph (10).

35 (B) Furniture, inventory, equipment used in the extraction  
36 process, or equipment used to store finished products that have  
37 completed the manufacturing process.

38 (11) "Tangible personal property" includes, but is not limited  
39 to, all of the following:

1 (A) Machinery and equipment, including component parts and  
2 contrivances such as belts, shafts, moving parts, and operating  
3 structures.

4 (B) All equipment or devices used or required to operate,  
5 control, regulate, or maintain the machinery, including, without  
6 limitation, computers, data processing equipment, and computer  
7 software, together with all repair and replacement parts with a  
8 useful life of one or more years therefor, whether purchased  
9 separately or in conjunction with a complete machine and  
10 regardless of whether the machine or component parts are  
11 assembled by the taxpayer or another party.

12 (C) Property used in pollution control that meets or ~~exceeds~~  
13 *exceeds* standards established by this state or any local or regional  
14 governmental agency within this state.

15 (D) Special purpose buildings and foundations used as an  
16 integral part of the manufacturing, processing, refining, or  
17 fabricating process, or that constitute a research or storage facility  
18 used during the manufacturing process. Buildings used solely for  
19 warehousing purposes after completion of the manufacturing  
20 process are not included.

21 (E) Fuels used or consumed in the manufacturing process.

22 (F) Property used in recycling.

23 (c) No exemption shall be allowed under this section unless the  
24 purchaser furnishes the retailer with an exemption certificate,  
25 completed in accordance with any instructions or regulations as  
26 the board may prescribe, and the retailer subsequently furnishes  
27 the board with a copy of the exemption certificate. The exemption  
28 certificate shall contain the sales price of the machinery or  
29 equipment that is exempt pursuant to subdivision (a).

30 (d) Notwithstanding any provision of the Bradley-Burns  
31 Uniform Local Sales and Use Tax Law (Part 1.5 (commencing  
32 with Section 7200)) or the Transactions and Use Tax Law (Part  
33 1.6 (commencing with Section 7251)), the exemption established  
34 by this section shall not apply with respect to any tax levied by a  
35 county, city, or district pursuant to, or in accordance with, either  
36 of those laws.

37 (e) (1) Notwithstanding subdivision (a), the exemption provided  
38 by this section shall not apply to any sale or use of property which,  
39 within one year from the date of purchase, is either removed from

1 California or converted from an exempt use under subdivision (a)  
2 to some other use not qualifying for the exemption.

3 (2) Notwithstanding subdivision (a), on or after January 1, 2011,  
4 the exemption established by this section shall not apply with  
5 respect to any tax levied pursuant to Sections 6051.2, 6051.5,  
6 6201.2, and 6201.5, or pursuant to Section 35 of Article XIII of  
7 the California Constitution.

8 (f) If a purchaser certifies in writing to the seller that the property  
9 purchased without payment of the tax will be used in a manner  
10 entitling the seller to regard the gross receipts from the sale as  
11 exempt from the sales tax, and within one year from the date of  
12 purchase, the purchaser (1) removes that property outside  
13 California, (2) converts that property for use in a manner not  
14 qualifying for the exemption, or (3) uses that property in a manner  
15 not qualifying for the exemption, the purchaser shall be liable for  
16 payment of sales tax, with applicable interest, as if the purchaser  
17 were a retailer making a retail sale of the property at the time the  
18 property is so removed, converted, or used, and the sales price of  
19 the property to the purchaser shall be deemed the gross receipts  
20 from that retail sale.

21 (g) This section ~~applies~~ *shall apply* to leases of tangible personal  
22 property classified as “continuing sales” and “continuing  
23 purchases” in accordance with Sections 6006.1 and 6010.1. The  
24 exemption established by this section shall apply to the rentals  
25 payable pursuant to such a lease, provided the lessee is a qualified  
26 person and the property is used in an activity described in  
27 subdivision (a). Rentals that meet the foregoing requirements are  
28 eligible for the exemption for a period of six years from the date  
29 of commencement of the lease. At the close of the six-year period  
30 from the date of commencement of the lease, lease receipts are  
31 subject to tax without exemption.

32 (h) This section shall cease to be operative on January 1, 2017,  
33 and as of that date is repealed.

34 SEC. 2. This act provides for a tax levy within the meaning of  
35 Article IV of the Constitution and shall go into immediate effect.